No. 76-226

In the Supreme Court of the United States

OCTOBER TERM, 1975

In Re CRATEO, INC.,

Bankrupt,

CRATEO, INC.,

Petitioner,

v.

INTERMARK, INC., et al.,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

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TOPICAL INDEX

TOPICAL INDEX (Continued)

CITATIONS

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The Petitioner, Crateo, Inc., respectfully prays that a Writ of Certiorari issue to review the judgment and opinion of the United States Court of Appeals for the Ninth Circuit.

OPINION BELOW

The opinion of the Court of Appeals for the Ninth District, not yet reported, appears in the Appendix. No opinion was rendered by the District Court.

JURISDICTION

The opinion and judgment of the United States Supreme Court of Appeals for the Ninth Circuit was entered on May 27, 1976 affirming a judgment of the United States District Court for the Southern District of California dated August 7, 1973 (____F.3d____). The United States Court of Appeals (Ninth Circuit) denied a timely petition for rehearing on June 28, 1976. The jurisdiction of this Court is invoked under 28 U.S.C. Section 1254(1).

QUESTIONS PRESENTED

1. Does a corporation commit the fifth act of bankruptcy by seeking State Court supervision over its voluntary dissolution where no appointment is made by the court of an indifferent person as a receiver?

2. Does a construction of Bankruptcy Section 3a(5) permitting conversion of the directors of a corporation into trustees for creditors without the consent of the directors, the consent of the shareholders, or the consent of the creditors:

a. Impose fiduciary duties to creditors upon directors without their consent and without "due process"?

b. Force directors into the servitude of creditors?

c. Deprive shareholders the control of the corporation without "due process"?

d. Deny creditors the right to have or select a disinterested receiver or trustee?

e. Place directors in jeopardy of both California law and Federal decisions which preclude "interested parties" such as directors, from acting as trustees?

3. What is the effect of presenting as a bona fide claim a judgment which represents 40% of the total claims and which is subject to attack for fraud?

4. Should a litigant be required to go to another forum to attack that fraud when concealment of the fraud took place in the court below and after a receiver has been appointed over the litigant's assets?

5. Is the statutory right to a jury trial denied where a Master (who is a Judge in the same district) is appointed who finds upon the ultimate question to be presented to the jury?

6. Is an installment judgment, or installment note, a "mature" debt in the bankruptcy sense as to installments not yet due?

STATUTORY PROVISION INVOLVED

Bankruptcy Act Section Three, 11 USC Section 21:

"a. Acts of bankruptcy by a person shall consist of his having. . . .

(5) while insolvent or unable to pay his debts as they mature, procured, permitted, or suffered voluntarily or involuntarily the appointment of a receiver to take charge of his property."

STATEMENT OF THE CASE

This petition raises questions concerning the interpretation of Section 3a(5) of the Bankruptcy Act and the use of a special master whose findings upon the ultimate issue in the case is given to the jury to take with them to the jury room.

Crateo, Inc. was a corporation which elected to voluntarily dissolve. Under California law, it was permitted to seek California Court supervision over the winding up process, which it did.

No receiver or trustee was appointed by the Court.

The California court, acting under statutory authority, issued a restraining order against creditors from litigating elsewhere, and required creditors to file their claims and proceed in that Court, thereby marshalling all litigation in that one court.

A Creditors' Petition in Involuntary Bankruptcy against Crateo was thereafter filed alleging that (1) Crateo was "unable to pay its debts as they mature" and (2) that by electing to dissolve and filing a Petition for Voluntary Dissolution it had the "legal effect to cause the Board of Directors to become 'Trustees' within the meaning of Section 3a(5) of the Bankruptcy Act." Crateo denied the petition.

At no time was any claim made by the creditors that Crateo's liabilities exceeded its assets, (insolvency). The only claim was that it was unable to pay its debts as they matured, (illiquidity).

After filing for dissolution Crateo continued to hold title to its assets, the directors got no title; the directors of Crateo continued to act as a Board of Directors and to run the business of Crateo; they filed no bond; they took no oath of loyalty to creditors; they continued to represent the shareholders; they obtained an injunction against the creditors; they

contested the involuntary petition in bankruptcy filed by the creditors; they filed four successive appeals and are before this Court.

In other words, the directors were, and continued to be, representatives of the shareholders, and were adverse, and continued to be totally adverse, to creditors. (The Ninth Circuit below on this point determined that even though there was no appointment by the State Court of a receiver or trustee to take charge of its property as required under Section 3a(5) of the Act, the mere seeking and receiving of the restraining order marshalling litigation before one Court under the California Statute, assuming inability to pay debts as they matured, amounted to the fifth act of bankruptcy.)

Crateo requested a jury trial. The District Court, however, referred the case to a judge who was a referee in bankruptcy in the same court system, and appointed him as a Master.

The Master made findings upon the ultimate question posed to the jury - whether Crateo, Inc. had debts which it was unable to pay as they matured. Those findings were not only read to the jury, but delivered in written form into the jury room without any request therefor by the jury. Cross examination of the Master was denied.

The Master's report made a formal finding that Crateo had $750,621.56 in 13 "debts" within the meaning of 3a(5) of the Bankruptcy Act. (*i.e.* that they were "mature.")

The so-called "mature" debts of Crateo discussed by the Ninth Circuit were:

(a)	Intermark Investing, Inc.	$229,848	30.6%
(b)	Southern National Bank of Houston	293,647	40.4%
(c)	Olympia Business Service	90,000	12.0%

The Intermark debt, constituting 30.6% of the entire sum found mature, arose from a stipulated "mixed" judgment for $229,848 calling for both "payment in installments" of only $5,000 per month and "performance." The judgment was secured by two parcels of property. Crateo, in addition, deeded the two parcels to Intermark.

Only one installment payment of $5,000 was owing to Intermark at the time of the involuntary bankruptcy petition. Since Intermark was secured by judgment lien and had deeds to the properties, it could have sold them and prepaid the installments of the judgment.

The Olympia Business Service debt (constituting 12% of the debt) was an installment note, the principal of which could be accelerated only upon 30 days' notice. The Master took note of the "notice" requirement, but failed to find that "notice" had been given. There is no testimony that such notice was given. Crateo contended that, absent notice, the principal was not mature, but that only two delinquent installments were mature.

The Master and the Ninth Circuit, despite the fact that unpaid installments were not due for either the Intermark installment judgment or the Olympia installment note, found the entire principal to be "mature." The Ninth Circuit used the word "fixed."

There was undisputed evidence upon which the jury could have found that Crateo, Inc. could pay its debts as they matured: Crateo, Inc. paid its non-disputed debts as they matured. (R.T. 282, line 3). It had over 800 vendor creditors who were constantly being paid. (R.T. 292, lines 1-3.) Crateo made deposits of $811,617.69 to its bank account at the end of August, September, October and November (R.T. 292-294). The balance sheet showed assets of $4,580,643 and total liabilities of $2,238,174. (R.T. 402, line 11). Finally, the creditors did not claim or allege insolvency.

POST-JUDGMENT

While the matter was pending on appeal, it was discovered that a judgment presented in evidence to show that Crateo, Inc. was unable to pay its debts as they matured, was procured by extrinsic fraud and concealment of an adjudication of forgery.

Southern National Bank of Houston had secured a judgment, not yet final, for not purchasing, as agreed, a promissory note purportedly issued to the bank by Toni Clark and others. The case is reported at 317 Fed.Supp. 1173 (July 29, 1970, Texas District Court). The note was never produced at the trial.

While that case was pending on appeal, and while the judgment thereon was being presented in the bankruptcy case below, the same plaintiff, Southern National Bank of Houston, in a Federal District Court in Nevada, suffered an adjudication that the purported signature of the maker, Toni Clark, was a forgery. This adjudication was concealed from the District Court in Texas and from the 5th Circuit, whose divided decision affirming, is reported at 458 Fed.2d 688, April 19, 1972, and from the Master and from the District Court below.

The claim for $293,647, founded on a forgery, constituted 40.4% of the claimed "mature" debt.

Appropriate and timely post-judgment motions were made and appropriate relief was sought. But all of those motions were met with the contention that the alleged bankrupt could not meet the issue in the Court below, where the proceedings were still alive, but must return first to Texas, where they were not, and seek to reopen there.

REASONS FOR GRANTING THE WRIT

I.

The Ninth Circuit Conflicts Squarely With The Second Circuit On Whether There Must Be (1) An Appointment; (2) By A Court; (3) Of An "Indifferent Person" In Order To Constitute An Act Of Bankruptcy Under Section 3a(5)

The Ninth Circuit, in its opinion below, stated relative to the Fifth Act of Bankruptcy:

> "There was no need for the Board of Directors to be formally appointed trustees or to formally possess legal title to the corporation's assets."

That opinion conflicts squarely with the opinion of the Second Circuit in *Blair & Co., Inc. v. Foley* 471 F.2d 178 (1972) which holds there must be an *"appointment" "by a Court"* of an *"indifferent person."*

In the Second Circuit case of *Blair & Co., Inc. v. Foley,* 471 F.2d 178 (1972) the court ruled that a private appointment of a liquidating agent by the stock exchange, while *Blair* was insolvent, did not result in commitment of the fifth act of bankruptcy. There had to be an appointment by a court of a receiver or trustee of an indifferent person between the parties to a cause.

The Supreme Court granted certiorari in 411 U.S. 930, 93 S.Ct. 1901, 36 L.Ed. 389 (73). It heard oral argument on November 12, 1973 but then dismissed the petition for mootness when the case no longer had a live controversy because the parties had accepted a Chapter XI plan. 414 U.S. 997.

The Second Circuit in *Blair* stated that what *Foley* presented as a policy argument was, in reality, a contention that

Congress made a wrong turn when it required creditors to establish an act of bankruptcy and did not permit the setting of the procedures of the Bankruptcy Act in motion by a showing of insolvency alone. *Blair, supra,* p. 184. Here the Ninth Circuit has gone the whole way by holding that a corporation which has neither assigned its assets to anyone nor had a trustee or receiver appointed has nevertheless committed the fifth act of bankruptcy which requires a receiver or trustee to be appointed to take charge of his property.

In the case below the corporation elected to voluntarily dissolve. California law provides that upon such procedure, the corporation's board of directors continues to act as a board, but is limited to such matters as winding up and dissolution. California Corporations Code 4800; 4801. California law provides that the Superior Court may supervise the winding up. Acting under that statutory authority, the Superior Court issued restraining orders requiring the creditors of Crateo, Inc. to litigate all their claims against Crateo, Inc. before the one Court.

The creditors alleging the fifth act of bankruptcy was committed, rested their contention upon the claim that the mere act of electing to dissolve plus the issuance of a restraining order by the Superior Court which marshalled the litigation into one court satisfied the requirement of Section 3a(5) of the Act that there be the appointment of a receiver or trustee to take charge of its property.

It is now appropriate to outline the history of the Act:

In the 1898 Bankruptcy Act, as amended in 1903, the language provided that an act of bankruptcy was committed where "because of insolvency, a receiver or trustee has been put in charge of this property under the laws of the state." Under that language the trustee did not have to be put in charge by an order of a court, but the language embraced all the other

methods by which the property of an insolvent is committed to a trustee for creditors under the laws of a state. *In re Hercules Atkins,* (D.C. Pa.) 13 Am. B.R. 369, 133 F. 813 (1904).

In the 1926 version of the Act, Congress provided alternative grounds for the act of bankruptcy. Thus, in 1926 the language of Section 3a(5) of the Bankruptcy Act read:

> ". . . while insolvent, a receiver or trustee has been appointed or put in charge of his property."

Under the 1926 Act either the appointment of a trustee or merely "the putting of a Trustee in charge" of his property sufficed for the Act of Bankruptcy.

In the 1938 version Congress completely eliminated that very language of "put in charge" which had been the subject of *In re Hercules Atkins, supra,* which the Court had construed as covering a trustee who had not been appointed by a court. In the 1938 version Congress firmly required that:

> ". . . while insolvent, or unable to pay his debts as they mature, procured, permitted or suffered voluntarily or involuntarily the appointment of a receiver or trustee to take charge of his property."

Under the 1938 Act, which governs this case, therefore, it is no longer sufficient to "put someone in charge." A trustee must have been "appointed to take charge of his property."

When Congress made its 1938 version of the Act, it had before it the earlier language and the interpretation of that language in such cases as *In re Hercules Atkins, supra,* the very sort of interpretation contended for by the Ninth Circuit below. This was the language which Congress eliminated in 1938 when it deleted the provision that an Act of Bankruptcy might be

committed where a receiver or trustee is "put in charge of his assets." This left as the exclusive method the "appointment" of a receiver or trustee. The language in the subjunctive permitting as an additional ground the putting of a receiver or trustee in charge, having been eliminated, the Congress was expressly nullifying the interpretation of that language as set forth in *In re Hercules Atkins, supra.*

2A Sutherland, on Statutory Construction, Section 45.12, page 37, states that judicial interpretation of statutes is conditioned by various conditional presumptions which the courts indulge in. This "legislative language will be interpreted on the assumption that the legislature was aware of existing statutes, the rules of statutory construction and judicial decision that if a change occurs in legislative language the change was intended in legislative result."

In support of the rule that "if a change occurs in legislative language a change was intended," Sutherland cites, among other cases, *People v. Valentine,* 28 Cal.2d 121, 169 Pac.2d 1 (1946).

In *People v. Valentine, supra,* the court held that where a statute with reference to one subject contains a given provision, the omission of such provision in a similar statute concerning a related subject is sufficient to show that a different intent existed. It is presumed that the legislature by deleting an express provision of a statute intended a substantial change in the law.

The inquiry then becomes: What did Congress mean when it required that the receiver or trustee be "appointed to take charge of his property?"

The term "appointment" means the designation of a person, by the person having authority thereof, to discharge the duties of some office or trust. *Orphant v. St. Louis State Hospital Div. of Mental Diseases* (Mo.) 441, SW2d, 355, at 360.

In *Blair, supra,* at 181, the Second Circuit stated:

> "It is undisputed that two of the conditions of Section 3a(5) were here fulfilled. *Blair* was insolvent or unable to pay its debts as they matured, and it permitted the appointment of Scorese to 'take charge' of its property in the ordinary meaning of that term. But that is not enough unless *Blair* permitted Scorese to be appointed as a 'receiver or trustee.'"
>
> "The liquidator did not meet what is usually regarded as essential to the status of a receiver, namely: Appointment by a Court."
>
> "A receiver is an indifferent person between the parties to a cause, or appointed by the court pendente lite when it does not seem reasonable to the court that either party should hold it. He is not the agent or the representative of either party to the action, but is uniformly regarded as an officer of the court."

Thus, the Second Circuit, in *Blair, supra,* holds that there must be an *"appointment" "by a court"* of an *"indifferent person."* It is obvious that the board of directors of Crateo, Inc. was not appointed by a court; it was not an indifferent entity. The board was the representative of the stockholders. It was not a neutral person. To the contrary, it vigorously opposed the creditors. Under the specific rule of *Blair, supra,* the petition of Crateo in dissolution could not constitute the appointment of a receiver to take charge of the property.

The Second Circuit in *Blair* further required that trustees have title to the property. Under the express ruling of *Blair, supra,*

the board of directors "lacked one element essential to the normal concept of trusteeship, namely: Legal title to the property." In this respect, the *Blair* case differs essentially from the Crateo case below and *In re Bonnie Classics, Inc.*, 116 F.Supp. 646 (S.D.N.Y. 1953) on which the Master in the court below mistakenly relied. As title to *Blair's* property did not pass to the liquidator he could not be a trustee. Similarly, under applicable California corporate law, title to a corporation's property remained with the corporation and it never became vested in the Crateo directors.

Since the essential element of passage of title is lacking the directors of Crateo never became "trustees." The Ninth Circuit, accordingly, also contradicts the Second Circuit on the issue of the necessity of "title."

Summing up:

The *Blair* case of the Second Circuit, rather than the *Crateo* case of the Ninth Circuit, appears more clearly to coincide with the intent of Congress and the wording of the 3a(5) Act in requiring:

1. an appointment;
2. by a court;
3. of an indifferent person.

II.

The Ninth Circuit Decision Which Permits Conversion Of Directors Into Trustees Or Receivers Without The Consent Of The Directors, The Shareholders And The Creditors, Creates Serious Constitutional Problems

The Ninth Circuit held that the effect of Crateo's actions (filing for dissolution) was to require its board of directors to act as trustees for creditors.

That opinion, however, ignores the facts that (1) the directors did not consent to act as trustees, (2) the shareholders did not

consent to have the directors act adversely to the corporation; (3) the creditors did not consent to have the directors act for them; (4) the directors took no oath of loyalty to creditors; in fact, they continued to act adversely to the creditors; and (5) the directors contested the involuntary petition filed by the creditors, filed four appeals, and now are petitioning this Honorable Court.

California Corporations Code Section 4800 states:

> "When voluntary proceedings for winding up or dissolution of a corporation have been commenced, *the board of directors shall continue to act as a board. . . .*"

California Corporations Code Section 4801 states:

> "The powers and duties of the directors after commencement of such proceedings include, but are not limited to, the following *acts in the name and on behalf of the corporation:*
>
> "(b) *To continue the conduct of the business* insofar as necessary for the disposal of winding up thereof."

The Ninth Circuit's opinion creates these profound constitutional problems:

1. Fiduciary duties to creditors would be imposed upon directors without "due process."

Under the Ninth Circuit's thesis Bankruptcy Section 3a(5) alters the California Corporations Code relative to directors. The directors would owe a "fiduciary duty" to the creditors forthwith upon filing the voluntary dissolution proceedings. Yet, clearly, the directors accepted no such fiduciary duty to creditors. To impose a "fiduciary duty to creditors" upon the directors contrary to the directors' wishes and without notice and hearing, violates the "due process" required by the 14th Amendment to the Constitution.

2. Directors would be forced into the involuntary servitude of the creditors.

The directors were elected by the stockholders and assumed office to serve the stockholders. They owe allegiance to the stockholders. To require those directors, without their consent, to serve the creditors, whose interests are adverse to the stockholders, imposes an involuntary servitude upon the directors in violation of the 13th Amendment of the Federal Constitution.

3. Shareholders would be deprived of control of the corporation without "due process."

To convert directors of corporations into trustees for creditors on filing of dissolution proceedings would deprive the shareholders of their control over the corporation and to that extent deny them of their property rights without "due process of law" and violate the 14th Amendment to the U. S. Constitution.

4. Creditors are denied their statutory right to select a trustee as provided by Section 44 of the Bankruptcy Act (11 U.S.C. Sec. 72).

Under Section 44 of the Act the creditors (exclusive of a corporation stockholders, officers or directors) have the right to make the appointment. It flies in the face of Section 44 to permit the corporation itself to make its directors the trustees by filing for dissolution. The creditors are denied their right to select a disinterested trustee.

5. Directors would be placed in civil jeopardy for violation of state law.

California Civil Code Section 566 precludes parties or persons interested in the action from being appointed receiver.

III.

The Ninth Circuit Conflicts With Both California Statute And The Eighth Circuit On The Need For A Disinterested Trustee.

After filing for dissolution the directors of Crateo continued to act as a board of directors and to run the business of Crateo; they filed no bond; they took no oath of loyalty to creditors; they continued to represent the shareholders; they obtained an injunction against the creditors; they contested the involuntary petition in bankruptcy filed by the creditors; they filed successive appeals; and they are before this Honorable Court.

The directors were, and continued to be, representatives of the shareholders; and were adverse, and continued to be totally adverse, and hostile to creditors.

The Ninth Circuit, however, held that after dissolution commenced:

> "The net effect of this change means that Crateo's actions in the State Court resulted in the 'appointment of a receiver or trustee' within the meaning of 11 USC Sec. 21(a)(5)."

The Ninth Circuit did not discuss the California Section which precludes "interested parties" from being appointed receiver or trustee, or the Eighth Circuit's holding in *R. J. Reynolds Tobacco Co., et al v. A. B. Jones Co., Inc. et al*, 54 F.2d 329 (1931) that a receiver should be without interest.

California Civil Code Section 566 recites:

> "no party . . . or person interested in the action . . . can be appointed receiver. . . ."

The Eighth Circuit in *R. J. Reynolds, supra,* recited at page 334:

> "A receiver in bankruptcy . . . should be entirely without interest or embarrassing

> connection so far as any party to the bankruptcy is concerned."

Then, speaking of the president and director of the bankrupt who had been appointed, the Eighth Circuit stated:

> "He had embarrassing connections, and would necessarily be regarded by the creditors as a hostile receiver."

We thus have this conflict that should be resolved. The Ninth Circuit in the Crateo case holds that interested parties (*i.e.* directors) notwithstanding their hostility to creditors, became converted into receivers or trustees for creditors; while the California State Law precludes interested parties from being appointed receiver; and, the Eighth Circuit holds receivers should be without interest.

IV.

The Opinion Of The Ninth Circuit Permitting Appellees To Benefit From Another's Fraud Is At Variance With The Opinion Of The Supreme Court.

After the trial below and after the Federal District Court had appointed a receiver for Crateo's assets, evidence emerged that one debt for $293,647, constituting 40% of the claimed mature debt presented to the jury, had been founded by a bank upon a forged note.

Upon discovery of the fraud, a motion was forthwith made to the Court to perpetuate testimony. It was denied and appealed. Thereafter, the record of the Nevada Court, in which the fraud was set forth, was obtained and a motion for new trial based on the newly discovered fraud was made. It too was denied and appealed.

The Ninth Circuit, in the case below, stated:

> "The bank, however, was not a party in Crateo's bankruptcy proceeding. The Texas judgment was merely introduced into evidence by other creditors of Crateo as tending to show Crateo was unable to pay its debts as they matured. There is no indication that any of those petitioning creditors knew of any possible irregularities connected with the evidence. Despite Crateo's protestations of fraud in the obtaining of the Texas judgment its Rule 60(b) motion in this case cannot be considered as falling under the third clause of that section because the bank's actions cannot be charged to any adverse party in the bankruptcy proceeding."

The effect of the Ninth Circuit opinion is 40% of the claims found to be "mature" by the Master were not due at all; that 40% amounted to $293,697. Yet they are used to thrust Crateo into bankruptcy.

The magnitude of that fraud is shown when juxtaposed with the facts that (1) Crateo had over 800 vendor creditors who were constantly being paid (R.T. 292, lines 1-3) and (2) Crateo was paying its non-disputed debts as they matured (R.T. 282, line 2).

The decision of the Ninth Circuit, shielding the creditors in their use of a judgment tainted by fraud amounting to extrinsic fraud is directly contrary to the decision of this Court in *Hazel Atlas Co. v. Hartford Co.*, 322 U.S. 238, 88 LE 250, 64 S.Ct. 997 (1944).

Under the Supreme Court's thesis the District Court below had the power to act directly upon those beneficiaries of the fraudulent judgment who are asserting rights based upon it.

In *Hazel Atlas, supra,* this court noted the general rule that courts are reluctant to alter judgments after the expiration of the

term at which judgments are finally entered, but that there has always existed, along side the term rule, another equity rule that certain circumstances, one of which is after discovered fraud, relief will be granted. The court then stated, at page 245:

> "Where courts have invoked the power relief has taken several forms: Setting aside the judgment to permit a new trial, altering the terms of the judgment, or restraining the beneficiaries of the judgment from taking any benefit whatsoever from it."

This is a most important appropriate case for the application of the rule of *Hazel Atlas, supra.*

The decision in *Southern National Bank of Houston v. Tri-Financial* (Crateo) cited at 317 Fed.Supp. 1173 (July 29, 1973) Texas District Court, was on appeal when *Southern National Bank* suffered a judgment in the District Court in Nevada that the signature of the maker of the note, Toni Clark, was a forgery. Had this matter been revealed to the Texas District Court, or to the Fifth Circuit where the case against *Tri-Financial* (Crateo, Inc.) was pending upon appeal, the case could have been reopened and the issue of the forgery and collateral estoppel could have come before the Texas Court when the case was not yet final. The Bank, however, did not reveal it. The Bank's attorneys - officers of the court - did not reveal it to any court.

It is clear that the *Southern National Bank of Houston,* having concealed the Nevada adjudication of forgery, could not use the prior Texas judgment with impunity or assert it in involuntary bankruptcy proceedings. The finality of the Texas judgment is attributable to its scheme of concealment. But here the case is live and the matter can be corrected.

The beneficiaries of that judgment, the petitioning creditors below, are seeking to take advantage of *Houston National Bank's* concealment of the adjudication.

The conduct of respondents, now that the fraud has been revealed, is exactly that characterized by the California Supreme Court as:

> "Attempting to profit from the wrong of another." *Moyle v. Landers*, 78 Cal. 99, 20 P. 241, 12 A.S. 122 (1889).

V.

Due Process Is Denied By Requiring An Entity To Attack Newly Discovered Fraud In Another Forum When (1) The Entity In Receivership Is Not Now Controlled By The Real Parties In Interest; (2) The Assets To Mount The Litigation Are Not In Their Control; (3) Discretionary Approval Of Court To Litigate Must First Be Had; (4) The Party Concealing The Fraud Appeared In The Court Below; And (5) The Concealment Of Fraud Was In Fact Perpetuated On The Court Below.

The Ninth Circuit, in dealing with the attempt to set aside the fraud, stated:

> "Crateo's post-judgment collateral attack on the Texas judgment was brought in the wrong forum."

That Ninth Circuit opinion *denies* Crateo *due process* for the following reasons:

1. It conceptually refers to "Crateo" as an entity without distinguishing between the former "corporation" and the new "entity in receivership."

2. Crateo "in receivership" is not controlled by its officers or directors. It is now controlled by the receiver.

3. Section 11C of the Bankruptcy Act specifically provides:

> "A receiver or trustee may, with the approval of the court, be permitted to prosecute as receiver or trustee any suit commenced by the bankrupt. . . ."

The litigation in the forum suggested by the Ninth Circuit could not take place by the parties prosecuting this appeal (*i.e.* the real parties in interest - the directors-shareholders of Crateo) since they had no standing to appear in any court other than the court below after the appointment of a receiver. Though cloaked in the name "Crateo" in these proceedings, they have no standing to use that "cloak" in another forum. Only a receiver or trustee has that standing.

4. Economically speaking, the assets with which to prosecute an action in another forum are in the receiver's hands. The Parties before this court are denied the economic resources of Crateo to contest the fraud in another forum. Effective litigation cannot be mounted if control of funds is in the hands of a receiver.

5. An attorney for the bank appeared in the San Diego courtroom of the U. S. District Court and audited Crateo's proceedings. That attorney failed to notify the court of the Nevada adjudication of forgery.

The Order appointing the receiver for Crateo, dated August 20, 1973, specifically recites: ("Also present and indicating support for the petition were the following attorneys representing creditors of Crateo." (It then set forth the name of the attorney appearing for the bank and the fact that he represented the bank.)

There are all the earmarks of an "appearance" in (a) the form of the bank being present as a creditor and being represented by attorneys; (b) indicating support; (c) being named in the Order appointing the receiver; and (d) withholding information, while present, of the Nevada Court dismissal on the basis of forgery.

6. The fraud of concealment of the forgery was committed in the court below by attorneys for the bank.

VI.

Petitioner Was Deprived Of Its Statutory Right To A Jury Trial By A Reference To A Master Who Found Upon The Ultimate Issues Of The Case. This Is Directly Contrary To The Decision Of This Supreme Court.

Crateo, Inc. made a timely jury demand below. The District Court thereupon referred the matter to a master who found the basic ultimate issue in the case: Whether Crateo, Inc. had debts which it was unable to pay when they matured. That is directly contrary to the decision of this Court in *LaBuy v. Howes Leather Co.*, 352 U.S. 249, 1 LE2d 290, 77 S.C. 309 (1957).

Even worse, the Master was a judge in the same District, and an officer and arm of the Court. He therefore imposed an "aura" or "imprimatur" on the findings which an ordinary litigant simply cannot dispel, no matter how sound his facts.

The District Court then carefully directed the jury to such an extent that there was no real jury trial:

1. It informed the jury that the case was complicated and that a master had been appointed.

2. It admonished the jury not to take notes.

3. It stated it would furnish the Master's Report to them in the jury room.

4. It refused to permit cross examination of the Master.

5. It furnished the Master's Report in the jury room.

6. The Master was identified in that Report as a Judge in that District.

7. The Master's Report contained "findings" on the ultimate facts.

The statutory right to a jury trial here was hopelessly compromised in a prejudicial manner in that:

a. The use of a Master here was unwarranted. The facts were not unusually complicated for a jury to comprehend.

b. Crateo was denied the opportunity to offer evidence on the need for a Master. The appropriate procedure would have been to allow Crateo to examine the Master to show to the Court that the evidence given before him was not so complicated as to be beyond the comprehension of the jury. See Fifth Circuit case of *Boyd Callan, Inc. v. U.S.* 328 F.2d 505 (1964).

c. Where the court is justified in making a reference to a master, because of some complicated fact issues, that reference should be carefully guarded so as not to invade the judicial process any more than is necessary to resolve the complicated issues which required the reference in the first instance.

d. A master should not be a judge or referee in the same district since that casts him in a position akin to a God in the eyes of the jury.

e. Fairness requires that cross examination of the master be permitted.

f. The master should, under no circumstances, be permitted to resolve the ultimate issue.

g. Fairness requires that the jury not be given the results of the master in such a manner as to bear the imprimatur of the court; telling the jury not to take notes; the Judge, rather than Master, reading the report, thereby precluding observation of demeanor; giving the report (an official document) to the jury to be taken into the jury room; permitting the report to find on the

ultimate facts, appointing a brother judge in the same district to be the master; referring to the master as judge; refusing to permit the judge-master to be cross examined.

The foregoing totality of acts denied Crateo its statutory right to a jury trial as is provided for in Section 19A of the Bankruptcy Act (11 USC Sec. 42a).

It is contrary to the opinion of this court in *LaBuy v. Howes Leather Co., supra.*

VII.

The Ninth Circuit Opinion Has Given Rise To A Serious Question Of Statutory Interpretation Of The Phrase "Inability To Pay Debts As They Mature." It Used The Term "Fixed" In Dealing With Installments Not Yet Due. It Conflicts With The Second Circuit Which Holds That Installments Not Yet Due Are Not Mature.

Crateo and Intermark had stipulated to an installment judgment for $232,466 payable at the rate of $5,000 per month. A judgment lien was recorded against two properties. The stipulation provided (1) this is an installment judgment; and, (2) Intermark and Crateo were to use their "best efforts" to sell the properties at the appraised price. It was a "mixed" judgment of "installments" and "performance."

Thereafter, a dispute arose between Crateo and Intermark because the stipulation was uncertain as to how the appraiser was to be selected. One installment payment of $5,000 had been made. One installment of $5,000 had been withheld because of the dispute, and this one installment was due at the cleavage date of the creditors petition.

To avoid dispute, Crateo deeded the two properties to Intermark with instructions to sell for any sales price it could get, and apply the proceeds to the debt.

The Ninth Circuit, in dealing with Intermark debt, stated:

> "Intermark Investing, Inc. was a judgment creditor of Crateo's pursuant to a stipulated judgment.....Part of the judgment provided that two parcels of property.....would be sold and the proceeds of the sale applied to reduce Crateo's debt to Intermark. A dispute arose over the manner in which the properties were to be appraised.....This was essentially a dispute over the manner in which the judgment would be satisfied and cannot obscure the fact that Crateo's liability to Intermark had already been *fixed.*" *In re Trimble Co.*, 339 F.2d 828 at 844 (3rd Cir. 1964).

The Ninth Circuit opinion that the entire Intermark obligation was "fixed" imports a word not found in the Bankruptcy Act and gives rise to a question of the statutory interpretation of the phrase "inability to pay debts as they mature" found in 3a(5). It focuses attention on the entire obligation rather than upon the amount presently due.

The error in the Ninth Circuit's opinion is that the total amount of an installment note may be "fixed." But that is tangential. The real issue is that any installments which are "not due" are simply "not mature."

The Second Circuit in *Government of the Virgin Islands v. Brown* 221 F.2d 402 (1955) recognized that:

> "Maturity, when applied to commercial paper, means the time when the paper becomes due and demandable. . . ."
>
> "When a note is made payable in installments . . . such installments as have become due and deemed to have matured." (221 F.2d 402 at 405).

Moreover, the Intermark stipulated judgment further could not be "mature" since it was a *"mixed" judgment* of both *"installment money"* and *"performance"* in that each party was to use its "best efforts" to sell the property.

Intermark, in not (1) using the two grant deeds given it, or (2) not selling at an execution sale, did not use its "best efforts" to sell the property. It did not perform. Since Intermark did not perform, neither the entire judgment, nor any installment, was mature.

The Ninth Circuit erred in interpreting the Bankruptcy Act so as to separate out the money portion of the "mixed judgment" and state it was "fixed."

Further, Intermark could have either sold the properties using the deeds or levied execution and prepaid the installments on the judgment.

Intermark has never affirmatively contended that the properties on which it had judgment liens were not of substantial value. It waived its security in the two properties by only $500. (Finding III i of the Third Report). The implication is that the difference of $229,348 found owing by the Master ($229,848 minus $500) was fully secured, and, therefore, fully recoverable. There was also unrebutted testimony that the two properties had a net equity of at least $210,000.

The error of the Ninth Circuit in looking at the whole obligation rather than the "installment" which is due is also demonstrated in the Olympia Business Service note relative to which the Court stated.

> "Under a promissory note to Olympia Business Service, Inc., Crateo was obligated to pay $1,200 per month . . . appellant did not make the payments due July 1, 1970, and August 1, 1970 . . .

> whether or not Crateo received proper notice so as to accelerate payment of the entire amount remaining on the promissory note is irrelevant because the two monthly installments were definitely due at the time the creditors petition was filed."

By use of the wording "two monthly installments were definitely due at the time the creditors petition was filed," the Appellate Court implies, but does not say, that the Master's finding of a $90,000 obligation by Crateo to Olympia Business Service was overreaching. Crateo did not receive notice of acceleration of the note.

Crateo was denied a fair trial by:

1. Submitting the whole $232,466 Intermark judgment to the jury, rather than, at most, the one $5,000 withheld installment which was "mature"; and

2. Submitting the whole Olympia Business Service note for $90,000 to the jury rather than the two installments for $1,200 each which were due and mature.

The Second Circuit's position of "maturity" ought to prevail over the Ninth Circuit's tangential concept of using the word "fixed" since something can be "fixed," yet not be due at this time.

VIII.

The Ninth Circuit Decision Below, If Allowed To Stand, Will Destroy California's Statutory Scheme Of Voluntary Dissolution Of Corporation.

The only reason for a corporation in voluntary dissolution to go to the Superior Court is to obtain injunctive relief *against* would-be claimants for "claims and demands against the corporation, whether due or not yet due, contingent or unliquidated, or sounding only in damages." (Cal. Corp. Code 4608).

Crateo and many other companies that desire to voluntarily dissolve, have unliquidated claims against them. The only way of getting those claims eliminated or reduced to liquidated amounts is through this court process. In effect it: (a) funnels the claims into one court and (b) speeds up the time in which they must be presented. In essence, the statute permits litigation to take place in one place. It is a kind of "wholesale," "one location" approach as opposed to a "retail," "many situs" approach.

It is another mode of orderly adjustment with creditors as contemplated and permitted by the United States Supreme Court in *United States v. Kras*, 93 S.Ct. 631 at 640, 409 U.S. 434, 34 L.E2d 626 (1973).

As Chief Justice Burger therein stated:

> "The bankruptcy court is but one mode of orderly adjustment with creditors; it is not the only one since many debtors work out binding private adjustment with creditors." *United States v. Kras*, 93 S.Ct. 631 at 640, (1973) (concurring opinion).

If creditors can argue that by filing such a voluntary petition the directors are converted into trustees for creditors because of Bankruptcy Act Section 3a(5), then no corporation is going to be willing to risk using that California Statute.

This means that instead of a swift liquidation in one place, corporations will have to creep along until litigation is completed and the various Statutes of Limitation on claims have expired. This can take many years.

This simply is not efficient for the economy; it is against sound commercial practice; it freezes money and talent in a lingering corporate entity instead of permitting it to flow to new entities that can use that talent and money; it denies the shareholders the use of their investment for the duration of the long, drawn-out process.

It is not efficient for the judicial system. It proliferates and drags on litigation in many places.

CONCLUSION

1. The Ninth and Second Circuits differ on the need for an "appointment" of a "receiver" by "a court."

2. Converting directors into trustees or receivers for creditors creates serious Constitutional problems.

3. The Ninth Circuit conflicts with California Statute and the Eighth Circuit on the need for a disinterested party to be the trustee or receiver.

4. The Ninth Circuit conflicts with the Supreme Court on the issue of benefiting from another's fraud.

5. Due process was denied by requiring fraud upon the court below to be attacked in another forum.

6. The Ninth Circuit, contrary to Supreme Court decision, denied the right to a jury trial by referral to a Master-Judge who found on ultimate issues.

7. The Ninth Circuit conflicts with the Second Circuit on the issue of the "maturity" of installments not yet due.

8. The Ninth Circuit decision will destroy California's Statute for the dissolution of corporations.

This Court should grant Certiorari to resolve the magnitude of conflicts.

Respectfully submitted,

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APPENDIX

UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

IN RE CRATEO, INC., Bankrupt.	FILED May 27, 1976 EMIL E. MELFI, JR. Clerk, U.S. Court of Appeals
CRATEO, INC., Appellant, vs. INTERMARK, INC., et al., APPELLEES.	Nos. 73-3208, 74-2088, 74-2615, and 75-3061 OPINION

Appeal from the United States District Court
for the Southern District of California

Before: KOELSCH and GOODWIN, Circuit Judges, and
WOLLENBERG* District Judge

WOLLENBERG, District Judge:

Crateo, Inc., a California corporation, was in the business of purchasing "sick" Companies. Its own health came into question in late summer of 1970, and its creditors initiated involuntary bankruptcy proceedings. After a jury trial on the question of its ability to pay its debts, Crateo was adjudicated a bankrupt.

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*Honorable Albert C. Wollenberg, United States District Judge, Northern District of California, sitting by designation.

While appeal from that judgment was pending, Crateo requested permission from the trial court to take depositions pursuant to Rule 27(b) of the Federal Rules of Civil Procedure. While its original appeal was still pending, Crateo also filed in the trial court two motions to vacate the adjudication of bankruptcy under Rule 60(b) of the Federal Rules of Civil Procedure. Appeals from the denial of all three post-judgment motions were consolidated with the primary appeal. 1/ Finding no merit in any of appellant's arguments, we affirm the adjudication of bankruptcy and decline to remand the case for any further proceedings.

I. Adjudication of Bankruptcy

In the summer of 1970, Crateo elected to wind up its affairs and voluntarily dissolve. On August 31, 1970, it filed a petition for judicial supervision of the winding up process with the Superior Court of the State of California for San Diego County. See California Corporations Code §4607. On that same day, the Superior Court ordered that notice of the dissolution proceeding be published and that all known creditors of Crateo be informed of the petition. In addition, the Superior Court ordered all creditor actions against Crateo enjoined and required all claims against Crateo to be presented in the dissolution proceedings. See California Corporations Code §§4608, 4616. Shortly thereafter, a creditors' petition was filed in the District Court alleging that Crateo had committed the fifth act of bankruptcy as defined by Section 3(a)(5) of the Bankruptcy act, 11 U.S.C. §21(a)(5).

1/

The appeal from the adjudication of bankruptcy is No. 73-3208. The appeal from the denial of permission to take post-judgment depositions is No. 74-2088. The appeals from the denials of the motions to vacate judgment are Nos. 74-2615 and 75-3061.

In accord with Section 19(a) of the Bankruptcy Act, 11 U.S.C. §42(a), Crateo requested a jury trial on the question of its insolvency. Prior to that trial, several issues, including the issue of Crateo's insolvency, were referred to the referee in bankruptcy sitting as a special master. The special master's report on the issue of Crateo's insolvency was read to the jury at trial. The jury subsequently found that Crateo was insolvent at the time it filed its petition for dissolution in the state court, and a judgment adjudicating Crateo a bankrupt was entered on August 9, 1973.

Appointment of a Receiver or Trustee

The petitioning creditors alleged that Crateo's petition in the state court for judicial supervision of its dissolution amounted to the fifth act of bankruptcy, 11 U.S.C. §21(a)(5). That section provides, in pertinent part, that:

> Acts of bankruptcy by a person shall consist of his having . . . (5) while insolvent or unable to pay his debts as they mature, procured, permitted or suffered voluntarily or involuntarily the appointment of a receiver or trustee to take charge of his property. 2/

California law governing the dissolution of corporations creates a significant change in the status of the corporation and its directors. We agree with appellant's creditors and the District Court that the net effect of this change means that Crateo's actions in the state court resulted in the "appointment of a receiver or trustee" within the meaning of 11 U.S.C. §21(a)(5).

2/

The definition of "persons" in 11 U.S.C. §1(23) makes this section applicable to corporations.

After a petition for dissolution is filed, the board of directors continues to operate the corporation in order to settle its affairs. Cal. Corp. Code §4800. However, directors may be removed by the superior court for reasons of "dishonesty, misconduct, neglect, or abuse of trust." Cal. Corp. Code §4614. The court can take such an action on its own initiative, and the normal prerequisite of a shareholder's suit is not required. *Cf.* Cal. Corp. Code §811.

The duties of the board of directors are also limited once the dissolution proceedings come under judicial supervision. The only business the corporation can carry on is that of winding up. Cal. Corp. Code §4605. In carrying out this task, the board of directors is invested with extensive powers. Cal. Corp. Code §4801. The powers of the board of directors, however, are not unlimited. The state court has the specific power to determine the manner in which claims are to be presented and settled and how shareholders' rights are to be determined. The court has the power to oversee the complete dissolution process and discharge the directors from their obligations after the process is completed. Cal. Corp. Code §§4608-11, 4617. In addition, the court has the general power to "make orders and adjudge as to any and all matters concerning the winding up of the affairs of the corporation." Cal. Corp. Code §4607.

In winding up the corporation's affairs, the first duty of the board of directors is to satisfy the corporation's debts and liabilities. Cal. Corp. Code §5000. In satisfying these obligations, the directors' powers under Cal. Corp. Code §4801 are circumscribed by the overall supervisory power of the Superior Court under Cal. Corp. Code §4607. If the directors do not settle the corporation's obligations properly, the court has the duty to vacate the directors' actions and to make the appropriate settlement itself. *In re Trinity Tractor Co.*, 3 Cal.App.3d 428, 440-441, 83 Cal.Rptr. 783, 791-792 (1970).

In addition, Crateo's creditors could no longer pursue their normal legal remedies against Crateo once the Superior Court accepted Crateo's petition for judicial supervision of its dissolution proceedings. Actions already begun were stayed by the Superior Court's order. Whether or not legal title to the corporation's assets passed into the possession of the board of directors became irrelevant because creditors could sue neither entity.

There was no need for the board of directors to be formally appointed trustees or to formally possess legal title to the corporation's assets. The effect of Crateo's actions in the Superior Court was to require its board of directors, under court supervision, to act as trustees. 3/ In determining whether a corporate dissolution under state law is the equivalent of the fifth act of bankruptcy, "it is the end result that counts." *In re Bonnie Classics,* 116 F.Supp. 646, 648 (S.D.N.Y. 1953). 4/

3/

This result is not changed by the additional possibility that a receiver may be appointed pursuant to California Code of Civil Procedure §§564, 565.

4/

Blair & Co., Inc. v. Foley, 471 F.2d 178 (2d Cir. 1972), *vacated and remanded for consideration of mootness*, 414 U.S. 212 (1973), is not to the contrary. That case involved a private arrangement between a brokerage firm and the New York Stock Exchange for the appointment of a liquidating agent for the firm. No court was involved in the liquidation process nor did the winding up process force creditors to forego their normal legal remedies. In light of the different factual situation herein, we need not comment further on the *Blair* case.

Not every corporate petition for dissolution under the California Corporations Code will necessarily result in an involuntary bankruptcy. Under 11 U.S.C. §21(a)(5), the creditors must also show that the debtor was "insolvent or unable to pay his debts as they mature." However, if this situation exists, California corporations cannot defeat the operation of the bankruptcy laws by applying for dissolution under California law. *In re Watts & Sachs*, 190 U.S. 1, 27 (1902). The overly technical approach to the interpretation of 11 U.S.C. §21(a)(5) urged by Crateo must be rejected.

Petitioning Creditors

The creditors' petition against Crateo was required by Section 59(b) of the Bankruptcy Act, 11 U.S.C. §95(b), to be filed by at least "three or more creditors who have provable claims not contingent as to liability." Six petitioning creditors 5/ presented evidence before the special master, and Crateo claims that none of them had claims "not contingent as to liability." Examination of the creditors' claims, however, shows that appellant is incorrect.

Intermark Investing Inc. was a judgment creditor of Crateo's pursuant to a stipulated judgment entered in a state court prior to the filing of the creditors' petition. Part of the judgment provided that two parcels of property owned by Crateo would be sold and the proceeds of the sale applied to reduce Crateo's debt to Intermark. A dispute arose over the manner in which the properties were to be appraised prior to their sale. This

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5/ Two of the original petitioning creditors and four intervening creditors presented evidence before the special master on this question. Under 11 U.S.C. §95(f), the intervening creditors took on the status of petitioning creditors. *3 Collier on Bankruptcy* ¶59.29 (14th ed. 1975).

was essentially a dispute over the manner in which the judgment would be satisfied and cannot obscure the fact that Crateo's liability to Intermark had already been fixed. *In re Trimble Co.*, 339 F.2d 838, 844 (3rd Cir. 1964).

Under a promissory note to Olympia Business Service, Inc., Crateo was obligated to pay $1200 per month. Since appellant did not make the payments due July 1, 1970, and August 1, 1970, Olympia was properly determined to be a creditor whose claim was not contingent as to liability. There was no need for Olympia to obtain a judgment against Crateo before it could achieve the status of a petitioning creditor under Section 59(b). *Denham v. Shellman Grain Elevator, Inc.*, 444 F.2d 1376, 1380 (5th Cir. 1971). Whether or not Crateo received proper notice so as to accelerate payment of the entire amount remaining on the promissory note is irrelevant because the two monthly installments were definitely due at the time the creditors' petition was filed.

General Electric Company held two promissory notes which had fully matured prior to August 31, 1970. Again, there was no need for General Electric to have obtained judgments on these notes in order to satisfy the requirements of Section 59(b). The fact that there was a dispute over Crateo's indebtedness on another separate obligation to General Electric is irrelevant. 6/

Use of Special Master's Report at Jury Trial

Under Section 19(a) of the Bankruptcy Act, 11 U.S.C. §42(a), Crateo was entitled to a jury trial "in respect to the

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6/ While it would not be helpful to discuss the claims of the three other petitioning creditors, we believe the District Court correctly held that their claims were not contingent as to liability.

question of [its] insolvency." 7/ Prior to that trial, the issue of Crateo's insolvency had been referred to the referee in bankruptcy sitting as a special master. The report of the special master was then read to the jury pursuant to Rule 53(e)(3) of the Federal Rules of Civil Procedure. Crateo contends that the procedure followed in this case violated its right to a trial by jury on the question of its insolvency.

Crateo first claims that reference to a special master was unwarranted because the issues were readily understandable by a jury. F.R.C.P. Rule 53(b) provides that "in actions to be tried to a jury, a reference shall be made only when the issues are complicated." 8/ The petitioning creditors had alleged that Crateo was bankrupt because it could not pay its debts as they matured. While every claim of this type does not require use of a master, considering Crateo's tangled financial affairs and the duplication of those problems in two subsidiary corporations that had been merged into Crateo three days before the filing

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Although 11 U.S.C. §42(a) also gives debtors the right to a jury trial on the question of whether they committed an act of bankruptcy, there was no need for a jury trial on that issue in this case. Crateo did not dispute the fact that it had filed a petition for judicial supervision of dissolution in the state court. Crateo only disputed the legal effect that could be attached to its action.

8/

The trial was held in June of 1973. General Order in Bankruptcy No. 37 was in effect at that time and made Rule 53 of the Federal Rules of Civil Procedure applicable to jury trials in bankruptcy cases. *Cf. Diamond Door Co. v. Lane-Stanton Lumber Co.*, 505 F.2d 1199 (9th Cir. 1974). The Federal Rules of Civil Procedure with respect to masters now apply to bankruptcy proceedings because of Bankruptcy Rule 513.

of the petition in state court for judicial supervision of dissolution, we believe that there was no abuse of discretion in reference to the special master. Since this was a matter for the district judge's determination in light of his perception of whether the jury would find the issue complicated, Crateo's request to examine the special master on the complexity of the case was properly denied.

At the trial, the findings of the special master were read to the jury. In providing that these findings are "admissible as evidence" and "may be read to the jury," Rule 53(e)(3) does not require the special master to personally read the findings to the jury. Consequently, contrary to appellant's position, the special master did not have to be made available for cross examination on the procedures used to reach the findings presented to the jury.

The expert qualifications of the special master were Crateo's primary guarantee that the proper legal standards and procedures were used by the master in determining his findings. In this respect, it is significant that Crateo did not object to the qualifications of the master appointed in this case. 9/ At the trial, Crateo was given a full opportunity to introduce evidence that would contradict the findings of the special master and argue to the jury that the findings were incorrect. The jury was instructed on the role of the special master and the weight to be given to his report, and Crateo did not object to this instruction.

The procedures employed in the trial would not impermissibly interfere with the right to trial by jury guaranteed by the Seventh Amendment. *Ex parte Peterson*, 253 U.S. 300 (1920);

9/

Crateo was not prejudiced by the fact that the special master happened to be a federal bankruptcy referee.

Burgess v. Williams, 302 F.2d 91 (4th Cir. 1962). Crateo's statutory right to a jury trial under the Bankruptcy Act gives it no greater rights than those available in civil proceedings governed by the Seventh Amendment. *Diamond Door Co. v. Lane-Stanton Lumber Co.*, 505 F.2d 1199 (9th Cir. 1974). Under all the circumstances of this case, we conclude that Crateo received a fair and proper trial on the question of its insolvency.

Jury Instructions

The petitioning creditors had alleged and were required to prove that Crateo was "unable to pay [its] debts as they mature" when it petitioned for a judicially supervised dissolution in state court. 11 U.S.C. §21(a)(5). This is the "equity" definition of insolvency. The trial judge's instruction to the jury followed the language of the statute. 10/ Crateo objected to this instruction, claiming that the word "debts" is in the plural and therefore the creditor must show the debtor's inability to pay "substantially all" of its debts and not just the debtor's inability to pay "one or two or three" debts.

The words "unable to pay [its] debts as they mature" are contained in a statutory context which necessitates rejection of Crateo's argument. A debtor commits the fifth act of bankruptcy when he is unable to pay his debts as they mature *and* a receiver or trustee is appointed to take charge of his property. 11/

10/ The jury was instructed that "considering only those items which you have concluded are both debts and are mature, you must decide whether Crateo, Inc. had the ability to pay these debts on August 31, 1970."

11/ Thus, contrary to the implications in Crateo's argument, debtors are not thrown into bankruptcy merely because they cannot pay a few small debts at a particular moment.

In that situation, there is a good possibility that some creditors may not be able to recover their claims on an equitable basis with other creditors unless they are able to invoke the protections of the Bankruptcy Act. Without those protections, the fact that some, or even most, of the creditors could be paid is of little consolation to those who cannot be paid. Adoption of Crateo's position would be completely contrary to the increasing amount of protection afforded to creditors by successive revisions of 11 U.S.C. §21(a)(5). 12/ In addition, Crateo's proposed test would be so indefinite as to be unworkable. The trial judge properly declined to modify his instructions.

II. Motions to Vacate the Adjudication of Bankruptcy

Approximately eight months after judgment was entered adjudicating Crateo to be a bankrupt, and while the appeal from the judgment was pending, Crateo filed a motion in the District Court to vacate the judgment under Rule 60(b) of the Federal Rules of Civil Procedure. Because of the pending appeal, the District Court had no jurisdiction to enter an order under Rule 60(b). The most the District Court could do was to either indicate that it would "entertain" such a motion or indicate that it would grant such a motion. If appellant had received such an indication, its next step would have been to apply to this Court for a remand. *Canadian Ingersoll-Rand Co. v. Peterson Products*, 350 F.2d 18, 27-28 (9th Cir. 1965).

In this case, however, the District Court found that it was inappropriate to either grant or entertain the Rule 60(b) motion. This was only a procedural ruling and not a final determination of the merits of the Rule 60(b) motion. Such an order is not appealable. Crateo's "appeal" from the District Court's order

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12/ See 1 *Collier on Bankruptcy* ¶3.501 (14th ed. 1974).

must therefore be considered as a motion for remand of the case for consideration of the Rule 60(b) motion. *Weiss v. Hunna*, 312 F.2d 711, 713 (2d Cir. 1963) *cert. denied*, 374 U.S. 753 (1963); *Canadian Ingersoll-Rand Co. v. Peterson Products, supra*, 350 F.2d at 27 n. 16. We decline to order such a remand.

The basis of Crateo's motion was an attack upon the validity of a judgment from the United States District Court for the Southern District of Texas in favor of the Southern National Bank of Houston and against Crateo. See *Southern National Bank of Houston v. Tri Financial Corporation*, 317 F.Supp. 1173 (S.D. Tex. 1970), *affirmed sub nom. Southern National Bank of Houston v. Crateo, Inc.*, 458 F.2d 688 (5th Cir. 1972). This judgment was introduced as evidence tending to prove that Crateo was unable to pay its debts as they matured and comprised a large proportion of Crateo's unpaid debts. In its Rule 60(b) motion, Crateo claimed that the Texas judgment was obtained by fraud and should not have been considered at Crateo's bankruptcy trial.

The District Court in Texas had determined that Tri Financial, a predecessor of Crateo, was obligated to purchase a promissory note from the bank. While that decision was on appeal to the Fifth Circuit, the bank brought an action against one of the signers of the note in the United States District Court for the District of Nevada. After the defendant in the Nevada action raised the claim that her signature on the note had been forged, the bank decided not to prosecute its suit and the case was dismissed. The Fifth Circuit's decision came after the events in Nevada.

The bank, however, was not a party in Crateo's bankruptcy proceeding. The Texas judgment was merely introduced into evidence by other creditors of Crateo as tending to show Crateo was unable to pay its debts as they matured. There is no indication that any of those petitioning creditors knew of any possible irregularities connected with the evidence. Despite

Crateo's protestations of fraud in the obtaining of the Texas judgment, its Rule 60(b) motion in this case cannot be considered as falling under the third clause of that section because the bank's actions cannot be charged to any adverse party in the bankruptcy proceeding. 13/

The jurisdiction of the District Court in Texas over the parties in *Southern National Bank of Houston v. Tri Financial Corporation, supra*, was not challenged in the bankruptcy proceedings, and the petitioning creditors were entitled to rely on the judgment's presumptive validity. Crateo's post-judgment collateral attack on the Texas judgment was brought in the wrong forum. 14/

In its Rule 60(b) motion, Crateo also claimed that the bank had received some payments on the promissory note and that Crateo's indebtedness to the bank was therefore less than

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13/ Assuming that the inability to collect from one of the alleged signers of the promissory note eliminated Tri Financial's obligation to purchase the note from the bank, any possible fraudulent conduct in this situation would consist of the bank not informing the Fifth Circuit of the invalidity of the obligation before it affirmed the judgment of the District Court in Texas.

14/ The bank's Nevada action terminated in June of 1971, and the trial on the issue of Crateo's insolvency did not take place until June of 1973. Crateo first raised this issue in early 1974 when it moved for an order perpetuating testimony pending appeal. No satisfactory explanation of the delay in producing evidence of the Nevada action is provided. The possibility that it may have been too late to petition either the Fifth Circuit or the District Court in Texas to set aside their judgments does not allow Crateo to collaterally attack the judgment in this proceeding.

the amount stated in the Texas judgment. Again, the collateral attack on a presumptively valid judgment was brought in the wrong forum.

We also decline to remand the case because of Crateo's second Rule 60(b) motion. All of the pertinent information that is the basis for this motion should have been known to Crateo well before the 1973 trial on the issue of its insolvency. There is no excuse for waiting over two years after entry of judgment before filing this motion. 15/

III. Perpetuation of Testimony Pending Appeal

While the appeal from the adjudication of bankruptcy was pending, Crateo requested permission, pursuant to Rule 27(b) of the Federal Rules of Civil Procedure, to depose an officer of the Southern National Bank of Houston. This testimony was allegedly needed to investigate the circumstances surrounding the purported forgery on the promissory note and the satisfaction of the note discussed in part II, *supra*. The order denying Crateo's motion is an appealable order. *Ash v. Cort*, 512 F.2d 909 (3rd Cir. 1975). *Cf. Martin v. Reynolds Metals Corporation*, 297 F.2d 49 (9th Cir. 1961).

On appeal, we must decide whether there was an abuse of discretion by the trial court. *Ash v. Cort, supra.* For the reasons stated previously in part II, *supra*, Crateo could not collaterally attack the Texas judgment. There was, therefore, no reason in this bankruptcy proceeding to take depositions on the subject. Crateo's motion was properly denied.

15/ Many of the arguments raised by Crateo with respect to these two Rule 60(b) motions are irrelevant to the motions and are attempts to reargue the primary appeal. This is not the proper function of a Rule 60(b) motion.

The judgment in No. 73-3208 and the order in No. 74-2088 are affirmed. The appeals in Nos. 74-2615 and 75-3061 are dismissed. Considering Nos. 74-2615 and 75-3061 as motions to remand to permit the district judge to consider appellant's Rule 60(b) motions, the motions are denied.